

LOS ANGELES COUNTY BAR ASSOCIATION PROFESSIONAL RESPONSIBILITY AND ETHICS COMMITTEE

OPINION NO. 489: April 28, 1997

SUMMARY

A lawyer may not include in a retainer agreement language which limits a client's right to recover punitive or non economic damages in a malpractice action against the lawyer. A lawyer may not require the client to retain the lawyer in a Third Party action as a condition to recovering damages against the lawyer arising out of the Third Party claim.

AUTHORITIES CITED

Alderman v. Hamilton (1988) 205 Cal.App.3d 1033, 1037 [252 Cal.Rptr. 845]

In re Matter of Fonte (1994) 2 Cal. State Bar Ct.Rptr. 752, 760

Fracasse v. Brent (1972) 6 Cal.3d 784 [100 Cal.Rptr. 385]

General Dynamics Corp. v. Superior Court (1994) 7 Cal.4th 1164 [32 Cal.Rptr.2d 1]

Madden v. Kaiser Foundation Hospitals (1976) 17 Cal.3d 699, 706-08 [131 Cal.Rptr. 882]

Manatt, Phelps, Rothenberg & Tunney v. Lawrence (1984) 151 Cal.App.3d 1165, 1174 [199 Cal.Rptr. 246]

Merenda v. Superior Court (1992) 3 Cal.App.4th 1, 10 [4 Cal.Rptr.2d 87]

California Civil Code §1717(A)

California Rules of Professional Conduct, Rule 3-400

COPRAC Formal Opinion 1989-116

FACTS AND ISSUES

The Committee has been asked for an opinion whether it is ethically permissible for a law firm to include language in its standard retainer agreement which would condition and limit its liability to its clients. The proposal consists of the following language:

A. In a dispute, either party shall only be entitled to recover their actual monetary damages (including our unpaid attorney fees). Neither party shall be entitled to recover any punitive, speculative, indirect, or emotional damages.

B. If the dispute relates to any claim against you by third parties, a condition precedent to our liability is our representation of you to defend against the claim. If we are successful, we would be paid our normal hourly rates. If we are unsuccessful, we would not be entitled to any payment for our services in defending against the claim.

DISCUSSION

A. Proposal "A" is not Permissible as Drafted

The functional effect of Paragraph A of the proposal is to limit the law firm's exposure for non-economic (emotional distress) and punitive damages.¹ Although the provision is phrased as applying to both client and lawyer, the evenhandedness is illusory because clients have the right to terminate the lawyer-client relationship at any time without financial penalty. Fracasse v. Brent (1972) 6 Cal.3d 784, 781 [100 Cal.Rptr. 385].

California Rules of Professional Conduct, Rule 3-400(A) absolutely prohibits a lawyer from entering into a "contract with a client prospectively limiting the member's liability to the client for the member's professional malpractice;" See In re Matter of Fonte (1994) 2 Cal. State Bar Ct.Rptr. 752, 760 (1995 WL 92387). It is the Committee's opinion that a contract proposal which limits the kind or amount of damages a client could recover from a lawyer is a limitation of the lawyer's liability and is thus barred by Rule 3-400.

Certain limits on a lawyer's liability have been enacted by the Legislature.³ A primary example is a contractual arbitration clause. The use of arbitration as a method of resolving legal malpractice claims has been found not to violate Rule 3-400. See California State Bar Standing Committee on Professional Responsibility and Conduct [COPRAC], Formal Opinion 1989-116 (holding that there is no prohibition against a lawyer-client retainer agreement requiring arbitration of potential malpractice claims).⁴ The critical fact relied upon by COPRAC was the perceived neutrality of arbitration and the public policy of this state in favor of arbitration. COPRAC noted that malpractice claims are arbitrated in the medical field and that this practice was approved in Madden v. Kaiser Foundation Hospitals (1976) 17 Cal.3d 699, 706-08 [131 Cal.Rptr. 882]. See Formal Opinion 1989-116, at 2 (1989 WL 253-264, *2); see also Manatt, Phelps, Rothenberg & Tunney v. Lawrence (1984) 151 Cal.App.3d 1165, 1174 [199 Cal.Rptr. 246] (noting "strong public policy in favor of arbitration as a speedy and relatively inexpensive means of dispute resolution").

With respect to the applicability of Rule 3-400, COPRAC took the position that a legal malpractice arbitration clause did not limit liability in any meaningful way. Such a provision is neutral neither "detract[ing] fro [n]or limit[ing] an attorney's duty to use reasonable care... It merely selects the forum in which liability will be determined." Formal Opinion, 1989-116, at p. 3 (1989 WL 253264, *3). Law firm relies on this language contending that its proposal merely "delineates the procedural framework for any claims by either party." However, as noted above, it is the Committee's Opinion that law firm's proposal is neither evenhanded nor directed to the method by which a legal malpractice claim will be resolved. The plain terms of the proposed language would limit the amount of damages the client could recover in a malpractice action. Such language cannot be squared with the absolute prohibition contained in rule 3-400. The proposed language would directly favor the law firm's economic interests over those of the client and thus violate a primary condition underlying Formal Opinion 1989-116, at n2 (1989 WL 253264, *6).⁵

Finally, we note that the paragraph, as drafted, is misleading. The reference to "our" attorney fees implies that only the law firm would recover its unpaid legal fees as "actual monetary damages" if it was successful in a dispute with its client.⁶ This is incorrect. Under California law, a contractual attorneys fees provision is construed to benefit both parties to the contract even if, as written, it unilaterally favors only one of the parties. See Cal. Civil Code §1717(A). It is the public policy of this state that attorney fee agreements be fair and drafted in a manner which clients should reasonably be able to understand. Cf. Alderman v. Hamilton (1988) 205 Cal.App.3d 1033, 1037 [252 Cal.Rptr. 845] (noting statutory protections enacted by legislature). Attorneys have a professional responsibility to ensure that fee agreements are neither unreasonable nor written in a manner that may discourage clients from asserting any rights they may have against their attorney.

B. Proposal B Constitutes an Impermissible Restraint on the Client's Right to Choose Counsel

Paragraph "B" of the proposed addition to the law firm's retainer is understood by the Committee to address a situation where the law firm represented a client and in connection with that representation a third party is now suing the client for damages. The situation is ripe for a malpractice action by the client against the law firm alleging that the law firm is ultimately responsible for any loss sustained by the client as a result of the third party's lawsuit. The proposed language would require the client to retain the law firm to represent the client in the third party action as a condition to a separate action against the law firm for the client's damages arising out of the earlier representation and the third party lawsuit. It is the Committee's opinion that Paragraph B improperly restrains a client's right to counsel of its choice.

As noted previously, the client's right to discharge a lawyer with or without cause is nearly absolute; General Dynamics Corp. v. Superior Court (1994) 7 Cal.4th 1164, 1173-74 [32 Cal.Rptr.2d 1]; Fracasse v. Brent (1972) 6 Cal.3d 784, 790 [100 Cal.Rptr. 385]; Cal. Code Civ. Proc. §284; COPRAC Formal Opinion 1994-134 (1994 WL 200778 *1) (noting that client should have both "the power and the right to discharge his [or her] attorney with or without cause"). "No client should be forced to suffer the representation by an attorney in whom that confidence and trust lying at the heart of the fiduciary relationship has been lost." General Dynamics Corp. v. Superior Court (1992) 7 Cal.4th 1164, 1174 [32 Cal.Rptr.2d 6]. The Committee

believes that it is fully consistent with these authorities that a law firm cannot force a lawyer-client relationship upon a client or condition the client's decision as to which counsel to employ by the loss of a valuable right - the right to sue a lawyer for legal malpractice. (Cf. Merenda v. Superior Court (1992) 3 Cal.App.4th 1, 10, 4 Cal.Rptr.2d 87, noting that requiring lawyers to perform competently protects a client's economic interests).

Paragraph B of the proposal constitutes an improper restraint on a client's right to counsel of its choice. Therefore, we do not address whether it may create a conflict of interest for the lawyer, if the lawyer who is potentially subject to a legal malpractice action by the client, represents the client in a matter tied to the potential malpractice action. Nor do we address whether Paragraph B constitutes an impermissible limitation of liability in violation of Rule 3-400.

This Opinion is advisory only. The Committee acts on specific Inquiries submitted ex parte. The Committee's Opinions are based only on such facts as are set forth in the Inquiries submitted.

¹ The reference to non-recovery of "speculative" damages does not appear to be objectionable since such damages are not recoverable in any event. "[T]he mere probability that a certain event would have happened, upon which a claim for damages is predicated, will not support the claim or furnish the foundation of an action for such damages." Campbell v. Magana (1960) 184 Cal.App.2d 751 [8 Cal.Rptr. 32]; Williams v. Wraxall (1995) 33 Cal.App.4th 120, 130-131 [39 Cal.Rptr.2d 658]. The reference to "indirect" damages is more problematic since the term is undefined and has no accepted definition. Fee agreements are rigorously reviewed by courts and ambiguities or uncertainties will normally be construed against the lawyer. See Reynolds v. Sorosis Fruit Co. (1901) 133 Cal. 625, 630 [66 P. 21]; Severson & Werson v. Bolinger (1992) 235 Cal.App.3d 1569, 1572 [1 Cal.Rptr.2d 531]; Cal.Civ. Code §1654.

² In an appropriate case, a client may recover emotional distress damages as part of a legal malpractice claim (see Holliday v. Jones (1989) 215 Cal.App.3d 102, 119 [264 Cal.Rptr. 448] as well as punitive damages (see, Kluge v. O'Gara (1964) 227 Cal.App.2d 207 [38 Cal.Rptr. 607]. See generally 2 Ronald Mallen & Jeffrey Smith, *Legal Malpractice*, §19 (4th ed. 1996).

³ For example, California recently enacted legislation permitting lawyers to practice in Limited Liability Partnerships and thus avoid vicarious liability for malpractice committed by another lawyer in the law firm. Cal. Corp. Code §§15047 et seq.

⁴ A malpractice arbitration agreement requires the client's informed consent. See Formal Opinion 1989-116, supra; cf. Lawrence v. Walzer & Gabrielson (1989) 207 Cal.App.3d 1501 [256 Cal.Rptr. 6] (arbitration clause in fee agreement was not ethically improper but unenforceable nonetheless when the client has not knowingly agreed to the provision). Because we find that the provision proposed by law firm is improper under Rule 3-400, we do not address the issue of informed consent.

⁵ We note that outside the professional context of the lawyer-client relationship, limitation of liability provisions are freely enforced when they are fair and the product of arms-length bargaining. Nunes Turfgrass, Inc. v. Vaughan Jacklin Seed Co. (1988) 200 Cal.App.3d 1518, 1540 [246 Cal.Rptr. 832]. That freedom is restricted as applied to lawyers, who are members of a licensed profession with fiduciary obligations.